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SUBJECT

PANAMA ECONOMIC BRIEF NUMBER ONE: EMPLOYMENT TREND DURING THE ECONOMIC CRISIS

CLASSIFICATION

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PAGE 3

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TREASURY K-1

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566-2716

STATE B

SUE SACRINO INR

647-5213

8727

STATE B

RICHARD DOTSON ARA/PAN

647-4982

1915

STATE O

RICHARD WYROUGH ARA/PAN

647-6614

4915

STATE B

JOHN HARRINGTON ARA/ECP

647-4643

3234

STATE B

DICK BOGOSIAN EB/OMA

647-9497

4830

STATE B

DAVID W. NORLAND EB/IFD/OMA

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ERIC LUFTMAN ARA/ECP

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JOHN LOVAAS AID/LAC/CEN

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REMARKS:

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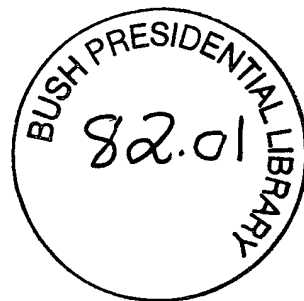
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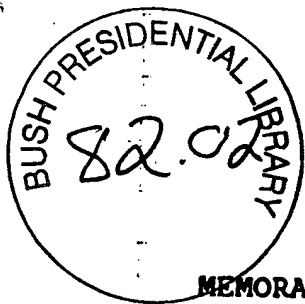
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MEMORANDUM TO: Recipients

The attached is the first of a series of economic .
briefs we hope to produce on Panama as the US and the new
government begin the task of economic reconstruction. This
one is on unemployment. We plan to follow it with looks at
capital flight and the banking sector. ☐

I hope you find this useful. If you have any questions
or comments, or if you have suggestions for other topics,
please call me ☐

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2 January 1990

MEMORANDUM

SUBJECT: Panama Economic Brief Number One: Employment Trends During the Economic Crisis

Panama's unemployment rate has almost doubled since 1987, largely due to the economic contraction that followed the imposition of economic sanctions by the United States against the government of Gen. Manuel Noriega (Table 1). The majority of the roughly 95,000 workers added to Panama's unemployment roles since 1987 probably came from three sectors: commerce, manufacturing, and construction. Employment in the two largest sectors in Panama--agriculture and government--has not declined significantly since the crisis began.

Economic Background

Commercial activity dropped significantly between 1987 and 1989, primarily as a result of less government income and spending, a decline in available credit, and a fall in general business confidence. The imposition of sanctions by the United States in April 1988 caused over \$350 million dollars in Panama Canal tolls and fees, income taxes from US firms operating in Panama, and bank assets to be withheld from the Panamanian economy. A run in March 1988 forced Panamanian banks to restrict cash withdrawals and reduce lending activity. Political upheaval and lack of confidence in Panama's stability as a business center led offshore banks to re-book assets in other financial centers, and caused international businesses to take employment-generating capital elsewhere.

Commerce

This sector is Panama's third largest employment generator, with over 93,000 laborers in 1986 (Table 2). Since 1987, production in this sector has fallen by over 40 percent (Table 3). Government expenditures during the crisis were limited to salary payments because of sharp drops in revenue, and private sector purchasing activity declined because of a lack of credit and postponed investment decisions. Inventories fell 2.5 percent on average in 1989, and that businesses were reducing general, administrative, and sales

costs, including labor. Anecdotal reporting suggests a general drop in disposable income encouraged many to eat at home instead of in restaurants. Average hotel occupancy has fallen considerably since 1987, the result of an uncertain political climate in Panama, and a precipitous drop in business and banking activity by foreigners.

Manufacturing

Manufacturing in Panama is largely geared to supplying domestic needs, and its 62,500 (1986) workers are therefore vulnerable to drops in domestic purchasing. Production in the manufacturing sector fell 28 percent between 1987 and 1989. In addition to the effect of a drop in consumption of manufactured goods, employment was affected by the slowdown in production caused by bank credit constraints. One example of the decline in manufacturing is the textile industry, which by mid-1988, had let all but 700 of its 4,000 workers go. Employment in the manufacturing sector will rebound as businesses begin to restock inventories and consumers resume purchases of domestically produced goods such as clothing, beverages, and tobacco.

Construction

The lack of credit availability, falling government spending, and an unfavorable climate for business expansion caused a 72 percent production drop in the construction sector between 1987 and 1989. The roughly 34,000 workers employed in this industry in 1986 have been directly affected by nearly non-existent construction activity.

War damage repairs and investment in infrastructural projects neglected by Noriega could quickly re-employ several thousand construction workers.

Other Sectors

Unemployment has also increased in the banking sector, which employs about 10,000 Panamanian workers. Hiring by financial institutions--primarily offshore banks--will likely resume as the domestic political situation stabilizes and as economic conditions allow them to offer competitive financial products and services to attract new business.

The Petroterminalas oil pipeline, while showing a drop in production of 50 percent since 1987, is a highly capital intensive project and has little direct bearing on employment. The project employs only 400 workers full time, and contracts 400 additional workers to provide other needed services. The pipeline's chief benefit to the government is

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as a source of income for investment in other employment-generating projects.

The Colon Free Trade Zone has largely weathered the 30-month political crisis, serving as an economic bright spot for the Noriega regime. Employment in the Zone, which fluctuates with the volume of trade between Latin America and the rest of the world, has remained between 7,500 and 9,500 workers since 1986. Trade through the Zone will be disrupted temporarily because of an estimated \$10 million in war damage and looting losses, but the medium-term effect on Zone employment will be minimal. The Zone, the pipeline, and the Panama Canal--which employs about 12,000 Panamanians--have all increased in importance as a share of GDP since mid-1987, and probably will be the government's most reliable sources of income and employment during the coming year (Table 4).

Impediments to Employment

Panama's Labor Code, adopted in 1972 to advance workers' rights and regulate the conduct of employer-employee relations, is a serious impediment to the free movement of labor resources. The Code stipulates that an employee's salary may not be reduced under any circumstances. Provisions also call for very high severance payments in the event of dismissal. Furthermore, after two years of employment, a worker cannot be dismissed without a legal hearing into the reasons for severance. Larger firms are required to maintain a reserve to cover possible severance payments, and are obligated to continue such payments in the event of bankruptcy.

The Labor Code has served as a disincentive to hiring workers, and has failed to boost real wages. To remain competitive, companies have turned to substituting capital inputs for labor inputs. Real wages have remained stagnant since the Code was adopted, and the job market remains tight for new entrants into the labor force. Modifications to the labor code make good business sense, but have been resisted by Panamanian legislators who fear the political impact of exposing Panamanian labor to downward wage pressures.

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Table 1

Panamanian Census Bureau Employment Figures
1982-1989

<u>Year</u>	<u>Employed</u>	<u>Unemployed</u>	<u>Rate</u>
1982	561,064	51,502	8.4
1983	597,345	64,219	9.7
1984	613,937	68,795	10.1
1985	626,973	88,251	12.3
1986	643,827	75,747	10.5
1987	681,141	89,331	11.6
1988	643,500	141,264	18.0
1989 ¹	616,000	184,000	23.0

¹Projected

Data: State Department Reporting

Table 2

Panamanian Employment by Sector
(1986)

<u>Sector</u>	<u>Percent</u>	<u>Employees</u>
Agriculture, Forestry, Fishing	28.6	184,134
Government, Community Services	28.4	182,847
Commerce, Restaurants, Hotels	14.6	93,999
Manufacturing, Mining	9.7	62,451
Transportation	5.6	36,054
Construction	5.3	34,123
Finance, Insurance, Real Estate	4.0	25,753
Canal Area	4.0	25,753
Utilities	1.5	9,657
Other	.2	1,288

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Table 3

Panama: GDP by Sector
(\$ millions)

	1987	1989 ¹	% Change
Government Services	681.3	590.0	(13.4)
Canal	482.5	445.0	(7.8)
Finance and Real Estate	774.7	428.0	(37.8)
Agriculture	535.5	395.3	(26.2)
Other	483.9	390.5	(19.3)
Commerce, Restaurants, Hotels	609.0	355.8	(41.6)
Manufacturing	475.5	341.5	(28.2)
Transport and Communications	281.8	276.7	(1.8)
Utilities	191.4	213.5	11.5
Colon Free Zone	202.1	205.5	1.7
Pipeline	369.7	185.0	(50.0)
Construction	229.9	63.8	(72.2)
Total	5317.3	3890.6	(26.8)

¹Projected

Table 4

Panama: Share of GDP by Sector
(percent)

Sector	1987	1989 ¹	Change
Finance and Real Estate	14.6	11.0	(3.6)
Government Services	12.8	15.0	2.2
Canal	9.1	11.4	2.3
Other	9.1	10.0	0.9
Agriculture	10.1	10.2	0.1
Manufacturing	8.9	8.8	(0.1)
Commerce, Restaurants, Hotels	11.5	9.1	(2.4)
Transport and Communications	5.3	7.1	1.8
Colon Free Zone	3.8	5.3	1.5
Utilities	3.6	5.5	1.9
Pipeline	7.0	4.8	(2.2)
Construction	4.3	1.6	(2.7)

¹Projected